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EX PARTE OR LATE FILED

July 28, 1998

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FEDERAL COMMUNICATIONS COMMISSION
DEPT. OF THE SECRETARY

Kyle Dixon
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Office of Commissioner Michael Powell
Federal Communications Commission
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EX PARTE

Re: Petition of Ameritech Corporation to Remove Barriers to Investment in Advanced Telecommunications Capability, CC Docket No. 98-32; Petition of Bell Atlantic Corporation for Relief from Barriers to Deployment of Advanced Telecommunications Services, CC Docket No. 98-11; Petition of U S WEST Communications, Inc. for Relief from Barriers to Deployment of Advanced Telecommunications Services, CC Docket No. 98-26; Petition of the Association for Local Telecommunications Services for a Declaratory Ruling, CC Docket No. 98-78; Southwestern Bell Telephone Company, Pacific Bell and Nevada Bell Petition for Relief from Regulation Pursuant to Section 706 of the Telecommunications Act of 1996 and 47 U.S.C. § 160 for ADSL Infrastructure and Service, CC Docket No. 98-91; Competitive Telecommunications Association, Florida Competitive Carriers Association, and Southeastern Competitive Carriers Association, Petition for Declaratory Ruling or, in the Alternative, Comparable Carriers under Section 251(h) of the Communications Act, CC Docket No. 98-39; Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act, of 1934, as amended, CC Docket No. 96-149

Dear Mr. Dixon:

Pursuant to your request, this letter serves to clarify concerns of MCI Communications Corporation ("MCI") regarding the insufficiency of the record with respect to the proposed action of the Federal Communications Commission (the "Commission") to allow incumbent local exchange carriers ("ILECs") to create separate subsidiaries for the provision of data services.

Section 706 of the Telecommunications Act of 1996 gives the Commission the opportunity to examine the deployment of advanced capabilities and directs the Commission to exercise its authority to address any concern in a procompetitive way. In recent months, several

of the Bell Operating Companies ("BOCs") have sought forbearance pursuant to section 706 from some of the most procompetitive provisions of the Act -- sections 251, 271 and 272. These petitions have been placed on public notice by the Commission and the respective comment periods have now been completed. In addition, the Commission must now, pursuant to section 706(b), initiate by August 8, 1998, an inquiry into the deployment of advanced capabilities to all Americans. The tasks associated with these petitions and the statutory mandate are, indeed, considerable.

It has come to MCI's attention that the Commission is considering taking several actions with respect to section 706. However, one action, which we understand is being considered by the Commission, though not contemplated under the Act, will undoubtedly result in serious, though inadvertent, consequences for consumers anxious to reap the benefits of competition and new entrants as they pursue opportunities to provide data services. As we understand it, the Commission is prepared to adopt an interim order permitting the ILECs to establish section 272 compliant subsidiaries that would be allowed to provide DSL and other "advanced" data services, but the separate subsidiaries would not be subject to the requirements of section 251(c), at least with respect to the provision of network elements on an unbundled basis.¹ While we commend the Commission for its effort to resolve some of the difficulties that new entrants have encountered in their efforts to provide data and other local services, we have several significant concerns about the Commission's suggested course of action.

First, the Commission lacks the statutory authority to permit the ILECs to avoid their obligations under section 251(c) and the BOCs under section 271.² MCI has set forth the legal arguments in its comments in the various section 706 proceedings, as have an overwhelming

¹ Because MCI has not been privy to any details of the proposal which has only been described to it in general terms, MCI does not know the extent of the subsidiary's exemption from the section 251(c) obligations.

² Congress required BOCs to fully implement section 251(c), and to demonstrate compliance with section 271, in order to prove that local competition has been established before the BOCs obtain authority to provide in-region long distance services. This is because Congress recognized that a separate affiliate requirement, by itself in the absence of any meaningful competition, is not sufficient to prevent anticompetitive conduct as a practical matter. Therefore, BOCs cannot obtain section 271 authority based solely on the provision of in-region long distance services through a separate affiliate because this organizational safeguard is ineffective. For related reasons, section 10(c) prohibits forbearance from 251(c) requirements until they are fully implemented. No significant competition in local data services has emerged, and the record does not establish that any ILEC (BOC or non-BOC) has fully implemented section 251(c), even with respect to providing xDSL-capable loops as unbundled network elements or collocation.

number of industry, consumer, state and federal commenters.³ Second, should the Commission conclude otherwise, MCI does not believe that the Commission has adequately detailed the specific proposal for the ILEC subsidiary nor has it given interested parties a fair and reasonable opportunity to comment on an approach that would allow the ILECs to avoid the requirements of section 251(c) by creating an affiliate that complies with the requirements of section 272. While the issue of section 272 compliance was raised by Ameritech in its petition,⁴ it sought the Commission's forbearance from section 272--the exact opposite requirement now allegedly under Commission consideration. Equally important, the Commission has not sought or received comment on the costs and benefits, if any, of forbearing from enforcement of section 251(c) on an interim basis--again an approach that none of the BOC petitioners suggested. Third, MCI, and many others, have expressed concern that the current state of play for the implementation and enforcement of section 272 requirements, is insufficient to address the myriad of discriminatory actions that incumbents may undertake.⁵

As stated above, MCI contends that issuance of an interim order allowing the ILECs to obtain forbearance of section 251(c) requirements by placing their data services in a separate subsidiary is procedurally flawed.⁶ In the pending section 706 proceedings initiated by several of

³ See, e.g., Letter from Larry Irving, Secretary of the National Telecommunications and Information Administration to Chairman, William E. Kennard, dated July 17, 1998, at page 11, wherein Secretary Larry Irving of the National Telecommunications and Information Administration suggests that the Commission should first seek comment on whether a separate subsidiary approach is violative of the Act.

⁴ See Petition of Ameritech Corporation to Remove Barriers to Investment in Advanced Telecommunications Capability, CC Docket No. 98-32 (filed March 5, 1998) (Ameritech Petition).

⁵ In this instance, MCI believes that the Commission should seek comment on what the ILEC would have to demonstrate in terms of full implementation with respect to, among other things, unbundled network elements and collocation, before its data affiliate could be relieved of 251(c) obligations. Further, the Commission should seek comment on whether the Commission or the state public service commissions should determine whether the preconditions have been met -- and whether they are being satisfied after the data affiliate becomes operational.

⁶ The adequacy of notice depends on "whether the final rule is a 'logical outgrowth' of the proposed rule." Krooritzky v. Reich, 17 F.3d 1509, 1513 (D.C. Cir. 1994); accord Nat'l Mining Assn. v. Mine Safety and Health Admin., 116 F.3d 520, 531 (D.C. Cir. 1997); Small Refiner Lead Phase-Down Task Force v. EPA, 705 F.2d 506, 543 (D.C. Cir. 1983). In determining "whether the purposes of notice and comment have been adequately served," Nat'l Mining Assn., 116 F.3d at 531 (internal quotations and citations omitted), the courts inquire "whether the notice given affords exposure to diverse public comment, fairness to affected parties, and an

the BOCs, Ameritech was the sole petitioner that raised any issue concerning section 272, and it sought relief from section 272 requirements for its data operations. In its petition, Ameritech suggests that a parade of horrors will ensue if it were required to abide by the section 272 mandates. Indeed, Ameritech initiated its request for forbearance from the section by stating, “[t]he structural separation requirements of section 272 are another significant impediment to Ameritech’s investment in advanced telecommunications capability.” Ameritech Petition at 15. It continues by contending that the section 272 requirements are “inconsistent” with Congress’s mandate in section 706 to eliminate barriers to infrastructure investment to encourage such deployment. *Id.* Ameritech then takes exception with virtually every one of the Commission’s requirements for section 272 compliance.⁷ In the end, Ameritech contends that “saddling” its data services business with “stringent” separations requirements would significantly increase the cost of building advanced services networks and thus “dampen” Ameritech’s incentives to construct facilities. *Id.* at 16.

Because Ameritech sought not to apply section 272 requirements to its data business, but to avoid these requirements, commenters appropriately addressed only the core issue presented by its request--whether the Commission has statutory authority to forbear from section 272 pursuant to section 10 and Commission precedent.⁸ Interestingly, some ILECs raised concerns

opportunity to develop evidence in the record.” Ass’n of Am. Railroads v. Dep’t of Transp., 38 F.3d 582, 589 (D.C. Cir. 1994) (internal quotations and citations omitted). Notice is not adequate if “the interested parties could not reasonably have anticipated the final rulemaking from the draft [rule],” Nat’l Mining Assn., 116 F.3d at 531 (internal quotations and citations omitted), or if a new round of notice and comment would “provide commenters with their first occasion to offer new and different criticisms which the agency might find convincing.” Fertilizer Institute v. EPA, 935 F.2d 1303, 1311 (D.C. Cir. 1991) (internal quotations and citations omitted).

⁷ Ameritech argued that the requirement prohibiting the separate affiliate from sharing employees would require it to “establish and maintain inefficient, redundant operations.” Ameritech Petition at 16. Ameritech also contended that section 272 would “impede an Ameritech operating company’s ability to share administrative services with a data affiliate by requiring the operating company to make all such services available to unaffiliated services providers on the same rates, terms, and conditioned on which they provide the data affiliate.” *Id.* at 16. Ameritech’s opposition goes to the heart of the coordination between the two operations that MCI has opposed in other Commission proceedings implicating section 272 requirements.

⁸ See e.g., Comments of Teleport Communications Group, Inc., CC Docket No. 98-32 at 12 (filed April 6, 1998) (explaining that the Commission has already found in its Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act, of 1934, as amended, 11 FCC Rcd. 21905, 21947 ¶ 87) (1996) (Non-Accounting Safeguards Order), on recon., 12 FCC Rcd 2297 (1997), recon pending, petition for summary review in part denied, and

about Ameritech's request for relief.⁹ As a result, the commenters have not been given the opportunity to address the different and, indeed, inconsistent concept apparently under

motion for voluntary remand granted sub nom. Bell Atlantic v. FCC, No. 97-1067 (D.C. Circuit order filed May 7, 1997) on remand, 12 FCC Rcd 8653 (1997), order on remand aff'd sub nom. Bell Atlantic Telephone Cos. v. FCC, No. 97-1423 (D.C. Cir. December 23, 1997), "[i]f a BOC's provision of an Internet or Internet access service incorporates a bundled, in-region, interLATA transmission component provided by the RBOC over its own facilities or through resale, that service may only be provided through a section 272 affiliate, after the BOC has received in-region, interLATA authority under section 271"; Comments of Transwire Communications, L.L.C., CC Docket No. 98-32 at 18 (filed April 6, 1998) (section 272 should not be swept away just two years after enactment simply because the BOCs allege they can improve some interLATA services); Comments of the Public Service Commission of Wisconsin and the Indiana Utility Regulatory Commission, CC Docket No. 98-32 at 3 (dated April 3, 1998) (Ameritech's request implicates the scope of state proceedings on this question); Consolidated Opposition of ACSI, CC Docket Nos. 98-11, 98-26, 98-32 at 10 (Congress determined that section 272's safeguards would be necessary for three years after a BOC obtains section 271 approval; it is impossible to conceive that removal of these safeguards before any BOC has received section 271 approval would serve the public interest or promote competitive market conditions); Consolidated Opposition of WorldCom, Inc., CC Docket Nos. 98-11, 98-26, 98-32 at 9 (filed April 6, 1998) (the Act does not distinguish between packet-switched facilities and any other telecommunications services or facilities with respect to the obligations under sections 251, 271 and 272); Intermedia Communications, Inc., Comments Opposing Deregulation of Incumbent Local Exchange Carrier Data Networks and Services, CC Docket Nos. 98-11, 98-26, 98-32 at 26 (filed April 6, 1998) (section 706 cannot be interpreted to override the procompetitive provisions of the Act contained in sections 251, 252, 271 and 272); Opposition of the Competitive Telecommunications Association, CC Docket Nos. 98-11, 98-26, 98-32 at 16 (filed April 6, 1998) (section 272 forbearance cannot be granted until three years after the BOC receives section 271 authority); Opposition of the Association of Local Telecommunications Service, CC Docket Nos. 98-11, 98-26, 98-32 at 23 (filed April 6, 1998) (stating that the BOCs fail to address at all the important issue of allocation of investment, revenues and expenses, in the event the FCC were to grant their requested relief); Comments of the Internet Access Coalition, CC Docket Nos. 98-11, 98-26, 98-32 at 4 (filed April 6, 1998) (ISPs and CLECs must have a level playing field and a fair opportunity to compete, which makes safeguards essential (such as separation between ILEC and ISP affiliate, affordable access on similar terms and conditions).

⁹ GTE stated it did not believe that the statutory requirements of sections 271 and 272 can be indirectly overruled through forbearance. Comments of GTE, CC Docket Nos. 98-11, 98-26, 98-32 at 8 (filed April 6, 1998). While US West agreed that less onerous restrictions should be established for a separate affiliate, it nevertheless stated that many of its data services were being offered in a manner that would not be conducive to separate subsidiary operation. Comments of U S West, Inc., CC Docket Nos. 98-11, 98-32 at 5 (filed April 6, 1998).

consideration by the Commission. This distinction is critical. Because Ameritech's request was conditioned on a request for forbearance, commenters reasonably proceeded on the basis that the request could not be granted absent the conclusion that the Commission would forbear from enforcing the 251(c) obligations. As such, the commenters focused their comments on the question of whether forbearance is permissible under the statute, not the issue now under consideration -- an interim order allowing ILECs to create a separate subsidiary that is not subject to section 251(c) requirements because it would not be deemed an ILEC under section 251(h).

Moreover, the Commission has several proceedings wherein issues with regard to its rulings on section 272 compliance remain unresolved. Although the Commission has addressed section 272 compliance in its Non-Accounting Safeguards and Accounting Safeguards Orders,¹⁰ issues remain as a result of outstanding petitions for reconsideration. In fact, MCI has raised numerous issues in its petitions for reconsideration that go to the heart of the effectiveness of the Commission's rules promulgated pursuant to section 272.¹¹ Issues such as problems that arise when a parent company is exempt from section 272 requirements, the ability of the operating company to provide a wide range of administrative and other services to the affiliate, the risks associated with the affiliate's ability to provide local services free of the 251(c) obligations and the need for rules on collocation, performance reporting and brand names use by the subsidiary are just a handful of the very momentous questions that are now before this Commission and

¹⁰ Section 272 regulations and policies that the FCC has adopted require that the BOC will continue to comply with all of the requirements of 251(c) after the 272 affiliate goes into business. Changing that fundamental requirement, at a minimum, raises questions about whether and how the section 272 rules ought to be modified when the BOC -- and non-BOC ILECs -- can use the subsidiary to avoid compliance with 251(c) requirements.

¹¹ Numerous important practical questions still need to be addressed by the Commission if it concludes that ILECs are permitted to create a separate subsidiary for data services not subject to section 251(c) obligations. For example, the Commission must determine the functions the data affiliate would be authorized to provide as well as the equipment it could own and operate. It would also need to draw the line between equipment used for "advanced" data services and services that the ILEC will continue to provide as well as the equipment that can be used for both voice and data services. The Commission would also need to determine the specific reporting requirements that the ILEC would have to meet in order to demonstrate that the affiliate is not receiving preferential treatment; the consequences of ILEC failure to treat its data affiliate on reasonable and nondiscriminatory terms, the parameters of any joint marketing arrangements, and how the imputation requirement in section 272 would be interpreted and applied in the case of data subsidiaries.

which must be addressed.¹²

Some have suggested that the Commission may only be “clarifying” certain of its previous decisions.¹³ However, comment has not been sought on the question of section 272 compliant subsidiaries that will provide local exchange services.¹⁴ Clearly, granting ILECs authority to establish separate data affiliates that would not be subject to section 251(c) requirements, would exceed any Commission grant of ILEC authority to date. Further, if permitted, without the appropriate safeguards, MCI is convinced that there will be a devastating and insurmountable impact on the deployment of advanced capabilities and on competition in the advanced capabilities arena for years to come.

It is for the reasons set forth herein that MCI respectfully suggests that instead of granting interim relief, the Commission seek notice and comment on any proposal allowing an ILEC to be exempt from section 251(c) requirements with respect to data services as long as it provides

¹² In the Matter of Implementation of the Non-Accounting Safeguards of the Sections 271 and 272 of the Communications Act of 1934, As Amended, Petition for Reconsideration of MCI Telecommunications Corporation, CC Docket No. 96-149 (filed February 20, 1997).

¹³ Although the Commission has determined that a BOC affiliate need not be classified as an incumbent LEC under section 251(h)(1)(B)(ii) merely because it is engaged in local exchange activities, (See In the Matter of Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, As Amended, First Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-149, FCC 96-489, released December 24, 1996, at ¶ 312), it has not yet determined the circumstances under which such a subsidiary is or is not an incumbent under 251(h). The answer to this question is critical if the Commission determines that ILECs should be allowed to establish section 272 subsidiaries that are not subject to incumbent obligations under section 251(c).

¹⁴ In its recent petition, The Competitive Telecommunications Association requested a declaratory ruling that: (i) an ILEC that operates under the same or a similar brand name and provides wireline local exchange or exchange access service within the ILEC’s region will be considered a “successor or assign” of the ILEC under section 251(h)(1)(B)(ii) of the Act and consequently that the affiliate itself is subject to section 251(c) requirements; or (ii) in the alternative, that the FCC create a rebuttable presumption that an ILEC affiliate that provides wireline local exchange or exchange access service within the ILEC’s region under the same or similar brand name is a “comparable” carrier under 251(h) and subject to 251(c) requirements. See Competitive Telecommunications Association, Florida Competitive Carriers Association, and Southeastern Competitive Carriers Association, Petition for Declaratory Ruling or, in the Alternative, Comparable Carriers Under Section 251(h) of the Communications Act, CC Docket No. 98-39. Were the Commission to allow ILECs to establish affiliates for their data businesses, the Commission would in essence, predetermine this petition.

these services through a section 272 compliant subsidiary. Further, parties could be subject to an expedited comment period so that no party need be concerned that any delay would inhibit its ability to pursue market opportunities.¹⁵ In the end, we believe that this very crucial step will help the Commission to develop a more comprehensive record with respect to section 272 compliance by the ILEC separate affiliate and will assist the Commission when addressing the myriad of issues that must be considered in order to deter and remedy any potential anti-competitive behavior.

Sincerely,



Lisa B. Smith

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¹⁵ Nothing in the record provides any support for the conclusion that the ILECs would accelerate deployment of xDSL capabilities if they obtained interim relief. Some (but not all) of the ILECs make unsubstantiated claims that they will not make “innovative” investments because uncertainty about forbearance chills their willingness to do so. Interim relief still leaves substantial uncertainty. The Commission’s docket shelves are filled with ILEC assertions that innovation is being held hostage to a particular regulatory result. The Computer II proceeding, rate of return cases, and price cap regulation are all debates where the ILEC “innovation” argument has been made before.